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CHURCH OF SCIENTOLOGY INTERNATIONAL

UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

In re	)	Case No. 95-10911 aj
	)	
GERALD ARMSTRONG,	)	Chapter 7
	)	
Debtor.	)	Date: June 7, 1996
	)	Time: 10:00 a.m.
	)	Place: Courtroom of the
	)	Honorable Alan Jarislovsky
	)	

REPLY IN SUPPORT OF CHURCH OF SCIENTOLOGY INTERNATIONAL'S  
APPLICATION TO REQUIRE TRUSTEE TO ABANDON  
PROPERTY OF THE ESTATE PURSUANT TO 11 U.S.C. SECTION 554

At the time debtor Gerald Armstrong filed his petition for  
bankruptcy, Church of Scientology International ("the Church") was  
pursuing a claim against Armstrong and others in California Superior  
Court, Marin County Case No. 157680, for fraudulent transfer of  
assets, based on California's Uniform Fraudulent Transfer Act, Civil  
Code § 3439 et seq. That claim passed into the bankruptcy estate as  
an asset. The trustee has not pursued the claim and, in fact, does  
not oppose the Church's application that the claim be abandoned so  
that the Church, Armstrong's primary creditor, may pursue it. The  
only objection filed to the proposed abandonment is that of debtor



1       Armstrong argues, erroneously, that this Court has "already  
2 decided" the issue presented, and that, if it has not, the Court  
3 should preclude the Church (and, presumably, the Trustee) from  
4 pursuing the state court claims against third parties because that  
5 would, in some unspecified manner, interfere with his obtaining a  
6 "fresh start." Neither of these arguments are supported by either  
7 the record in this case or by law. Moreover, Armstrong does not have  
8 standing to object to the abandonment of the asset on the grounds  
9 presented. His "objections" are inappropriate regardless of whether  
10 the asset are pursued by the Trustee or by the plaintiff. The only  
11 objections which can properly be raised are those which would be  
12 raised by the Trustee on behalf of the estate and its creditors  
13 concerning the value of the asset and its collection -- and the  
14 Trustee has raised no objections.<sup>1</sup>

15       Section 554 of the Bankruptcy Code authorizes the Court to  
16 permit a trustee to abandon an asset of the bankrupt's estate if the  
17 property "is burdensome to the estate or ... is of inconsequential  
18 value and benefit to the estate." Here, there can be no doubt that  
19 the state court fraudulent conveyance claims are assets of the  
20 estate -- this court has so ruled, Order of May 25, 1995; see also,  
21 *In re Mortgageamerica Corporation*, 714 F.2d 1266, 1277 (5th Cir.  
22 1983) (holding that property fraudulently transferred under the  
23 Texas version of the Uniform Fraudulent Transfers Act remains  
24 property of the estate within the meaning of section 541(a)(1) of  
25 the Bankruptcy Code). Moreover, the trustee has made the  
26 determination that the asset falls within the categories described

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27  
28       <sup>1</sup>       The Church is not only Armstrong's primary creditor; it is the only  
creditor who has not received a re-affirmation of debt from Armstrong.



1 by section 554, by (1) making no effort to collect the asset; (2)  
2 consenting to abandonment of the asset; and (3) filing a final  
3 report without collection. Upon notice and hearing, this Court may  
4 consent to the abandonment, and permit the Church to proceed with  
5 the collection activity that the trustee has deemed too speculative.  
6 Following abandonment, the parties stand "as if no bankruptcy  
7 petition was filed" in relationship to the fraudulent conveyance  
8 claims. In re Dewsnap, 908 F.2d 588, 590 (10th Cir. 1990).

9 This Court has not previously decided the issues presented  
10 either by the Church's petition for abandonment, or by the  
11 underlying state court fraudulent transfer claims. Far from it. On  
12 May 25, 1995, this Court specifically reserved the fraudulent  
13 conveyance action, refusing to release it from stay, and  
14 acknowledging that it was an asset of the estate which only the  
15 trustee could pursue [Moving Papers at 2]. Nor did the adversary  
16 action brought by the Church address the fraudulent conveyance  
17 claims. That action addressed only the questions of whether  
18 Armstrong was entitled to discharge of his claimed debts, and  
19 whether the permanent injunction awarded to the Church by the state  
20 court was dischargeable. The assets of the bankrupts estate,  
21 including the state court claims, were not an issue, nor was the  
22 question of their potential collection or abandonment.

23 Armstrong attempts to confuse the bankruptcy question  
24 concerning dissipation of assets with the questions presented in the  
25 fraudulent conveyance action, arguing that the trustee and the  
26 Church are now collaterally estopped from pursuing the state court

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28 / / /



1 claims. However,

2 Under the doctrine of collateral estoppel, four  
3 criteria must be met before a determination is conclusive  
4 in a subsequent proceeding: (1) the issue sought to be  
5 precluded must be the same as that involved in the prior  
6 litigation; (2) that issue must have been actually  
7 litigated; (3) it must have determined by a valid and  
8 final judgment; and (4) the determination must have been  
9 essential to the judgment.

10 *Lovel v. Mixon*, 719 F.2d 1373, 1376 (8th Cir. 1983). Here, the  
11 parties involved, questions of law to be resolved, and the relevant  
12 evidence are all quite different in the state court action than in  
13 the bankruptcy court. The state court action is against transferees  
14 Michael and Sonia Walton, neither of whom were parties to the  
15 bankruptcy action. While dissipation in a six-year time period was  
16 not significant to this Court, transfers without compensation in  
17 1990 remain actionable under state law. Civil Code § 3439.09. Thus  
18 the consideration by this Court, peripherally, of some of the  
19 transactions that will be at issue in the state court action will  
20 not preclude or estop the resolution of that case.

21 Armstrong also asks the Court to preclude the Church from  
22 pursuing this asset of the estate, arguing that recovery by the  
23 Church of the property which he transferred to the Waltons would  
24 somehow preclude him from obtaining the "fresh start" which the  
25 bankruptcy affords to debtors. It is difficult, however, to see how  
26 the proceedings against the Waltons could impact negatively on  
27 Armstrong's fresh start -- unless, of course, Armstrong expects to  
28 be compensated by the Waltons, post-bankruptcy, for his fraudulent  
29 transfer. Even assuming arguendo that the state court action did  
30 impact on Armstrong in some fashion, that is not relevant to the

31 / / /



1 question of abandonment. According to the Ninth Circuit.

2 Impact on the debtor is not listed as one of the factors  
3 to be considered in authorizing abandonment, which suggests the  
4 impact on the debtor is not a necessary consideration. This  
5 makes sense in the context of the Bankruptcy Code as a whole.

6 *In re Johnston*, 49 F.3d 538, 541 (9th Cir. 1996).<sup>2</sup>

7 Armstrong has thus presented this Court with no cogent reason  
8 to refuse to permit the trustee to abandon the fraudulent transfer  
9 action, but merely with rhetoric intended to delay. The trustee has  
10 not opposed abandonment. The Church requests that the Court grant  
11 its application, so that the state court action may proceed to its  
12 final conclusion without further delay.

13 Dated: May 29, 1996

Respectfully submitted,  
WILSON, RYAN AND CAMPILONGO

14 By: Andrew H. Wilson  
15 Andrew H. Wilson

16 Laurie J. Bartilson  
17 MOXON & BARTILSON

18 Attorneys for Creditor  
19 CHURCH OF SCIENTOLOGY  
20 INTERNATIONAL

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26  
27 <sup>2</sup> Armstrong also argues that he believes the Church to be pursuing the claim  
28 against the Waltons for what he terms improper reasons. Armstrong's speculations  
are nonsense. The Church paid Armstrong more than half a million dollars, and  
seeks recovery of that loss.

PROOF OF SERVICE

I declare that I am employed in the City and County of San Francisco, California.

I am over the age of eighteen years and not a party to the within entitled action. My business address is 115 Sansome Street, Suite 400, San Francisco, California.

I am readily familiar with Wilson, Ryan & Campilongo's practice for collection and processing of correspondence for mailing with the United States Postal Service.

On May 29, 1996, I served the attached **REPLY IN SUPPORT OF CHURCH OF SCIENTOLOGY INTERNATIONAL'S APPLICATION TO REQUIRE TRUSTEE TO ABANDON PROPERTY OF THE ESTATE PURSUANT TO 11 U.S.C. SECTION 554** and **NOTICE OF HEARING ON CHURCH OF SCIENTOLOGY INTERNATIONAL'S APPLICATION TO REQUIRE TRUSTEE TO ABANDON PROPERTY OF THE ESTATE PURSUANT TO 11 U.S.C. SECTION 554** on the following in said cause, by placing for deposit with the United States Postal Service on this day in the ordinary course of business, true copies thereof enclosed in sealed envelopes. The envelopes were addressed as follows:

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I declare under the penalty of perjury under the laws of the State of California that the foregoing is true and correct.